

AMENDED IN ASSEMBLY MARCH 30, 2011

AMENDED IN ASSEMBLY MARCH 14, 2011

CALIFORNIA LEGISLATURE—2011–12 REGULAR SESSION

ASSEMBLY BILL

No. 229

Introduced by Assembly Member Lara

February 2, 2011

An act to amend Section 12410.5 of, to add Sections 12410.6, 12410.7, and 12410.9 to, and to add and repeal Section 12410.8 of, the Government Code, relating to audits.

LEGISLATIVE COUNSEL'S DIGEST

AB 229, as amended, Lara. ~~The~~ Controller: audits.

Existing law requires the Controller to superintend the fiscal concerns of the state. Existing law requires the Controller to receive every audit report prepared by any local agency to comply with the federal Single Audit Act of 1984.

This bill would require the audit reports prepared in this regard to be submitted to the Controller within 9 months of the end of the period audited or in accordance with applicable federal law. This bill would authorize the Controller to appoint a qualified certified public accountant to complete an audit report if it is not submitted by the local agency within the required timeframe, with associated costs to be borne by the local agency, as specified. This bill would require the audit to comply fully with the Government Auditing Standards issued by the Comptroller General of the United States. This bill would require the audits to be made by a certified public accountant that is licensed by the California Board of Accountancy and selected by a local agency from a directory of accountants to be published by the Controller by December 31 of

each year. The Controller would be required to use specified criteria to determine those certified public accountants that are to be included in the directory.

This bill would require the Controller to develop a plan to review and report the financial and compliance audits of local agencies, *and to review and monitor the audit reports performed by independent auditors, according to specified criteria*. This bill would require the Controller, in consultation with specified entities, to propose and adopt the content of an audit guide. This bill would also require the Controller to report to the Legislature by January 31 of each year the results of the ~~controller's~~ *Controller's* oversight activity. The requirement that the Controller report to the Legislature would be repealed on December 31, 2015.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

1 SECTION 1. The Legislature finds that financial audits provide
2 an independent assessment of, and reasonable assurance about,
3 whether local agencies' reported financial condition, results, and
4 use of resources are presented fairly in accordance with recognized
5 standards. Accordingly, it is the intent of the Legislature to promote
6 accountability over local government funding by establishing a
7 process for reviewing and reporting on financial and compliance
8 audits conducted of local agencies. It is further the intent of the
9 Legislature that the Controller shall have oversight responsibilities
10 for implementing and ensuring compliance with this act.

11 SEC. 2. Section 12410.5 of the Government Code is amended
12 to read:

13 12410.5. (a) The Controller shall receive every annual financial
14 audit report prepared for any local agency, as defined in Section
15 ~~53980~~ 53890, including those reports prepared in compliance with
16 the federal Single Audit Act of 1984 (P.L. 98-502; 31 U.S.C. Sec.
17 7501 et seq.) and required under any law to be submitted to any
18 state agency, and shall, after ascertaining its compliance with that
19 federal act, transmit the report to the designated state agency.

20 (b) An audit for any local agency submitted to the Controller
21 pursuant to this section shall comply ~~fully~~ with the Government

1 Auditing Standards issued by the Comptroller General of the
2 United States.

3 (c) An audit for any local agency submitted to the Controller
4 pursuant to this section shall be made by a certified public
5 accountant, licensed by the California Board of Accountancy, and
6 selected by the local agency, as applicable, from a directory of
7 certified public accountants deemed by the Controller as qualified
8 to conduct audits of local agencies which shall be published by
9 the Controller not later than December 31 ~~of each year. The~~
10 ~~certified public accountant shall possess individual education,~~
11 ~~examination, and experience qualifications that have been~~
12 ~~determined by the board to be substantially equivalent to the~~
13 ~~qualifications under Section 5093 of the Business and Professions~~
14 ~~Code, and that are in accordance with subdivision (b) of Section~~
15 ~~27 of Title 16 of the California Code of Regulations necessary to~~
16 ~~perform the full range of accounting services, including signing~~
17 ~~attest reports on attest engagements. of each year.~~

18 (1) In determining ~~that which~~ certified public accountants shall
19 be included in the directory, the Controller shall use the following
20 criteria:

21 (A) The certified public accountants or public accountants shall
22 be in good standing as certified by the California Board of
23 Accountancy.

24 (B) The certified public accountants or public accountants, as
25 a result of a quality control review conducted by the Controller
26 pursuant to Section 12410.9, shall not have been found to have
27 conducted an audit in a manner constituting noncompliance with
28 ~~subdivision (c) of that section.~~

29 ~~(2) It is the intent of the Legislature to ensure that auditors and~~
30 ~~audit organizations maintain their independence in appearance and~~
31 ~~in fact by rotation of public accounting firms. Beginning with the~~
32 ~~2011-12 fiscal year, a local agency shall be prohibited from using~~
33 ~~the same public accounting firm to perform an annual financial~~
34 ~~and compliance audit for more than five consecutive years. The~~
35 ~~Controller may waive this requirement if he or she finds that no~~
36 ~~qualified auditor is otherwise available to perform the audit.~~
37 ~~subdivision (b) of this section and subdivision (a) of Section~~
38 ~~12410.7. The Controller shall establish an appeals process for~~
39 ~~certified public accountants or public accountants who are~~
40 ~~removed from the directory but not referred to the California Board~~

1 of Accountancy pursuant to subdivision (b) of Section 12410.7 or
2 subdivision (d) of Section 12410.9.

3 (2) Commencing with the 2011-12 fiscal year, it shall be
4 unlawful for a public accounting firm to provide audit services to
5 a local agency if the lead audit partner, or coordinating audit
6 partner, having primary responsibility for the audit, or the audit
7 partner responsible for reviewing the audit, has performed audit
8 services for that local agency in each of the six previous fiscal
9 years. The Controller may waive this requirement if he or she finds
10 that no otherwise eligible auditor is available to perform the audit.

11 (d) The governing board of each local agency shall include all
12 of the following in its contracts for audits:

13 (1) A provision to withhold 10 percent of the audit fee until the
14 Controller certifies that the audit report conforms to the reporting
15 provisions of subdivision (a) of Section 12410.7.

16 (2) A provision to withhold 50 percent of the audit fee for any
17 subsequent year of a multiyear contract if the prior year's audit
18 report was not certified as conforming to the reporting provisions
19 of subdivision (a) of Section 12410.7. This provision shall include
20 a statement that a multiyear contract shall be null and void if a
21 public accounting firm or independent auditor is declared ineligible
22 pursuant to subdivision (d) of Section 12410.9. The amount
23 withheld shall not be payable unless payment is ordered by the
24 board or the audit report for that subsequent year is certified by
25 the Controller as conforming to the reporting provisions of
26 subdivision (a) of Section 12410.7.

27 (3) A provision that will provide the Controller access to audit
28 working papers.

29 SEC. 3. Section 12410.6 is added to the Government Code, to
30 read:

31 12410.6. (a) The Controller shall develop a plan to review and
32 report on financial and compliance audits of local agencies. The
33 Controller, in consultation with the Department of Finance, and
34 representatives of the League of California Cities, the California
35 State Association of County Auditors, and the California Society
36 of Certified Public Accountants, shall propose the content of ~~and~~
37 ~~adopt, and adopt,~~ an audit guide.

38 (b) The audit reports shall be submitted to the Controller within
39 nine months after the end of the period audited, or in accordance
40 with applicable federal law.

(c) If the audit reports required by Section 12410.5 have not been submitted by a local agency to the Controller on or before the due date established by this section, the Controller ~~shall~~ *may* appoint a qualified certified public accountant to complete the report and to obtain the information required. Any cost incurred by the Controller pursuant to this subdivision, including contracts with, or the employment of, the certified public accountants in ~~compiling the audit report~~ *completing the audit* shall be borne by the local agency and shall be a charge against any unencumbered funds of the local agency.

SEC. 4. Section 12410.7 is added to the Government Code, to read:

~~12410.7. (a) To determine the practicability and effectiveness of the audits and audit guide, the~~

12410.7. (a) The Controller on an annual basis shall review and monitor the audit reports performed by independent auditors. The Controller shall determine whether the audit reports conform with the reporting provisions of subdivision (b) of Section 12410.9 government auditing standards and the audit guide and shall notify each local agency, and the auditor of each local agency regarding each determination.

(b) The independent auditor shall correct his or her audit report within 30 days of notification of any deficiency. The Controller may suspend the independent auditor from performing any local agency audits if the auditor does not correct his or her audit report within 30 days of the Controller's notification.

(c) *(1) Within 30 days from the date of receipt of written notification that the Controller refuses to certify an audit report as conforming to the reporting provisions described in subdivision (a), an independent auditor or audit firm having a portion of an audit fee withheld pursuant to paragraph (1) or (2) of subdivision (d) of Section 12410.5 may file an appeal in writing with the California Board of Accountancy.*

(2) The board shall complete an investigation of the appeal within 90 days of the filing of the appeal and, on the basis of the investigation, do one of the following:

(A) (i) Order the Controller to provide notification that the audit report conforms to the reporting provisions described in subdivision (a).

1 (ii) *If the board orders the Controller to provide notification*
2 *that the audit report conforms to the reporting provisions described*
3 *in subdivision (a), the Controller shall notify the contracting local*
4 *agency, which shall then release the portion of the audit fee being*
5 *withheld in accordance with paragraph (1) or (2) of subdivision*
6 *(d) of Section 12410.5.*

7 (B) *Schedule the appeal for a hearing, in which case the final*
8 *action on the appeal shall be completed by the board within one*
9 *year from the date of the filing of the appeal.*

10 SEC. 5. Section 12410.8 is added to the Government Code, to
11 read:

12 12410.8. (a) The Controller shall report to the Legislature by
13 January 31 of each year the results of the Controller's oversight
14 activity, including the results of the Controller's quality control
15 reviews.

16 (b) A report submitted pursuant to subdivision (a) shall be
17 submitted in compliance with Section 9795.

18 (c) Pursuant to Section 10231.5, this section is repealed on
19 December 31, 2015.

20 SEC. 6. Section 12410.9 is added to the Government Code, to
21 read:

22 12410.9. (a) The Controller may perform quality control
23 reviews of audit working papers to determine whether audits are
24 performed in conformity with government audit standards and the
25 local agency audit guide. The Controller shall communicate the
26 results of his or her reviews to the Department of Finance, the
27 independent auditor, and the local agency for which the audit was
28 performed, and shall review his or her findings with the
29 independent auditor.

30 (b) Prior to the performance of any quality control reviews, the
31 Controller shall develop and publish guidelines and standards for
32 those reviews. Pursuant to the development of those guidelines
33 and standards for those reviews, the Controller shall provide an
34 opportunity for public comment. The Controller shall update the
35 guidelines and standards for any changes in audit standards.

36 (c) The Controller is responsible for selecting audits for review
37 based on criteria, including, but not limited to, disciplinary actions
38 by the California Board of Accountancy, results of the Controller's
39 review and monitoring of the audit reports, the extent of findings
40 in the audit reports issued by the independent auditor, the number

1 of audits of local agencies performed annually by the independent
2 auditor, the independent auditor's experience in performing audits
3 of local agencies, the complexity of state and federal programs
4 administered by the local agencies, and requests or leads from
5 other sources.

6 (d) If the quality control review of the Controller indicates that
7 the audit was conducted in a manner that may constitute
8 unprofessional conduct as defined pursuant to Section 5100 of the
9 Business and Professions Code, ~~including, but not limited to,~~
10 ~~breach of fiduciary responsibility of any kind, gross negligence,~~
11 ~~repeated negligent acts resulting in a material misstatement in the~~
12 ~~audit or or repeated~~ failure to disclose noncompliant acts, the
13 Controller shall refer the case to the California Board of
14 Accountancy. If the California Board of Accountancy finds that
15 the independent auditor conducted an audit in an unprofessional
16 manner, the Controller may prohibit the independent auditor from
17 performing any audit of a local agency for a period of three years,
18 in addition to any other penalties that the California Board of
19 Accountancy may impose. In any matter that is referred to the
20 California Board of Accountancy, the Controller may suspend the
21 independent auditor from performing any local agency audit
22 pending final disposition of the matter by notice and an opportunity
23 to respond to that suspension. The independent auditor shall be
24 given credit for any period of suspension if the California Board
25 of Accountancy prohibits the independent auditor from performing
26 ~~audits of the local agency under subdivision (c). In any audits of~~
27 ~~local agencies. In any~~ event, the Controller shall not suspend an
28 independent auditor under this subdivision for a period of more
29 than three years.